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Losing Control: Why IMF Article VIII(2)(b) May Nullify the Enforceability of Financing Contracts When Spiraling Oil Prices Prompt the Use of Exchange Controls

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NOTES

LOSING CONTROL: WHY IMF ARTICLE VIII(2)(B) MAY NULLIFY THE ENFORCEABILITY OF FINANCING CONTRACTS WHEN SPIRALING OIL PRICES PROMPT THE USE OF EXCHANGE CONTROLS

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INTRODUCTION

As the price of oil continues its climb, a potential catastrophe looms on the horizon. While the countless effects of surging oil prices have been discussed at length, one possibility has received far less attention—the revival of International Monetary Fund[1] ("IMF") Article VIII(2)(b) as a defense to financing contracts. If the recent surge in oil price accelerates, countries may be forced to adopt new monetary policies to protect their own faltering currencies.

The effects of countries adopting new monetary policies,[2] especially currency exchange controls, might call into question the enforceability of many exchange and financing contracts.[3] Exchange controls can take the form of a limit upon the outflow of local currency, a limit on the outflow of U.S. dollars, or mandatory rates of exchange.[4] The IMF requires member states[5] to enforce each others' exchange controls when imposed consistently[6] with the IMF Articles of Agreement.[7] Specifically, Article VIII(2)(b) declares:

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1. "The IMF is an international organization . . . established to promote international monetary cooperation, exchange stability, and orderly exchange arrangements; to foster economic growth and high levels of employment; and to provide temporary financial assistance to countries to help ease balance of payments adjustment." IMF, About the IMF, *available at* http://www.imf.org/external/about.htm [hereinafter About IMF] (last visited Feb. 1, 2008).

2. Monetary policy refers to actions undertaken by a government, central bank, or monetary authority to "influence the availability and cost of money and credit to help promote national economic goals." Bd. of Governors of the Fed. Reserve Sys., Monetary Policy: Federal Open Market Committee, http://www.federalreserve.gov/monetarypolicy/fomc.htm (last visited Feb. 1, 2008).

3. These exchange controls can also be defended by the Act of State Doctrine and the Foreign Sovereign Immunities Act. *See generally* Stephen Zamora, *Recognition of Foreign Exchange Controls in International Creditors' Rights Cases: The State of the Art*, 21 INT'L LAW. 1055 (1987) (discussing how Sovereign Immunity and the Act of State Doctrine can be used as a defense in cases involving the adoption of exchange controls); *see also infra* notes 147-148 and accompanying text.

4. *See, e.g.*, Callejo v. Bancomer, S.A., 764 F.2d 1101, 1106 (5th Cir. 1985); *see also* note 22 and accompanying text.

5. Currently 185 countries are signatories of this agreement. *See* About the IMF, *supra* note 1.

6. Courts, particularly those less well-versed in the technicalities of foreign exchange regulations, may call upon the Executive Board of the IMF to assess whether the exchange control has been validly imposed. *See* International Monetary Fund, Articles of Agreement, Second Amendment, Apr. 30, 1978, T.I.A.S. No. 8937, 29

> Exchange contracts which involve the currency of a member and which are contrary to the exchange control regulations of that member maintained or imposed consistently with this Agreement shall be unenforceable in the territories of any member.[8]

This provision applies to both governments and private contracting parties in IMF member states where exchange controls are imposed.[9] Article VIII(2)(b) completely bars the enforcement of an illegal exchange contract in any IMF member state.[10] Although much ink has been spilled over what precisely comprises an "exchange contract," however, there is no international consensus.[11] The disagreement centers upon whether the term "exchange contract" should be viewed broadly or narrowly.[12] A broad interpretation, generally preferred by developing countries, would encompass any contract that involves monetary elements; a narrow interpretation, generally preferred by developed countries, includes only those contracts that contemplate the

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U.N.T.S. 2203, art. XXIX, *available at* http://www.imf.org/external/pubs/ft/aa/aa.pdf [hereinafter IMF Articles of Agreement]; s*ee also* Gerhard Wegen, *2(B) or Not 2(B): Fifty Years of Questions – The Practical Implications of Article VIII Section 2(B)*, 62 FORDHAM L. REV. 1931 (1994); *Callejo*, 764 F.2d at 1119 (noting that a legal opinion of the IMF is persuasive authority as to whether the exchange control has been imposed consistently with the Articles of Agreement). The "IMF's general interpretative view [is] that currency regulations should be presumed to be in conformity with the Fund Agreement unless the Fund indicates otherwise." *Id.* at 1119 n.25. *But see* Pan Am. Life Ins. Co. v. Blanco, 311 F.2d 424, 427-28 (holding that Cuba's exchange controls were not imposed consistently with the Fund Agreement, despite a legal opinion by the IMF, but providing no explanation as to why).

7. IMF Articles of Agreement, *supra* note 6; *see also* William W. Park, *When the Borrower and the Banker Are at Odds: The Interaction of Judge and Arbitrator in Trans-Border Finance*, 65 TUL. L. REV. 1323, 1351 (1991).

8. IMF Articles of Agreement, *supra* note 6, art. VIII(2)(b). The article has been enacted into U.S. law by 22 U.S.C. § 286(h) (1994) ("[T]he first sentence of article VIII, section 2(b), of the Articles of Agreement of the Fund . . . shall have full force and effect in the United States . . . .").

9. *See* Philip J. Power, Note, *Sovereign Debt: The Rise of the Secondary Market and its Implications for Future Restructuring*, 64 FORDHAM L. REV. 2701, 2743 (1996).

10. Allan T. Marks, *Exchange Control Regulations within the Meaning of the Bretton Woods Agreement: A Comparison of Judicial Interpretation in the United States and Europe*, 8 INT'L TAX & BUS. LAW. 104, 105 (1990).

11. Park, *supra* note 7, at 1351; *see also* Wegen, *supra* note 6 (explaining how different language translations of the article contributes to the lack of consensus).

12. *See, e.g.*, Park, *supra* note 7, at 1351-52; Wegen, *supra* note 6, at 1937-38.

exchange of one currency for another.[13] This lack of a precise definition leads to uncertainty in financing contracts between developed and developing countries, and can potentially destroy these contracts and even bankrupt companies.[14] In any case, parties on either side of a financing agreement can take measures to shield themselves from this uncertainty.[15]

Part I of this Note will investigate how a potential surge in the price of oil might cause developing countries to use more exchange controls. This part will also briefly examine the causes of a drastic surge in oil prices and how enacted exchange controls can destroy aspects of project financing. Part II will analyze what constitutes an "exchange contract" within the meaning of Article VIII(2)(b). Finally, Part III suggests various methods that may reduce the likelihood of Article VIII(2)(b) reeking havoc upon seemingly ironclad financing contracts. Various methods proposed include: an interpretation of the article directly from the IMF, explicit stipulation by the contracting parties regarding the exact interpretation of the article, and a choice of law provision included in the contract. In this age of uncertainty and sky-high oil prices, the best option is for the IMF to adopt an amendment to the Articles of Agreement.

I. OIL'S POTENTIAL FOR DEVASTATION

The record-high price of oil has countless effects on every facet of the global economy.[16] Higher oil prices lead to inflation and lower investment in oil-importing countries as the affected government and its

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13. *See* Libra Bank v. Banco Nacional de Costa Rica, 570 F. Supp. 870, 897 (S.D.N.Y. 1983) ("The narrow view of 'exchange contracts' . . . is that they are contracts for the exchange of one currency against another or on means of payment against another. The broad view is that they are contracts involving monetary elements."). It has been argued that any contract which, in any way, affects a country's exchange resources would fall into the "monetary elements" described in the broad interpretation. *Id.*

14. *See infra* Part II.

15. *See infra* Part IV.

16. *See generally* INTERNATIONAL ENERGY AGENCY, ANALYSIS OF THE IMPACT OF HIGH OIL PRICES ON THE GLOBAL ECONOMY (2005), *available at* http://www.iea.org/textbase/papers/2004/high_oil_prices.pdf [hereinafter IEA ARTICLE]; Gwynne Dyer, *The Oil Price*, GLOBAL BUS. NETWORK, May 14, 2004, http://www.gbn.com/ArticleDisplayServlet.srv?aid=27640 ("[I]t was soaring oil prices that triggered three of the past four global recessions . . . .").

citizens have less money to spend.[17] Oil price increases also alter the balance of trade and exchange rates between countries.[18] Oil-importing countries normally experience deterioration in their balance of payments,[19] which exerts downward pressure on their exchange rates and leads to higher inflation.[20] This combination of higher inflation, higher unemployment, lower exchange rates, and lower real output imposes pressure on the government to take appropriate action.[21] The response may take the form of exchange controls,[22] which tend to restrict the outflows of the local currency.[23]

Although the above-envisioned scenario requires a "perfect storm" of sorts, its likelihood increases every day as oil prices continue to climb. On November 6, 2007, oil futures closed at a high of $96.27 per barrel,[24] a 40% surge over the previous three months[25] and just short of

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17. IEA ARTICLE, *supra* note 16, at 6.

18. *Id.*

19. Balance of payments is commonly defined as a measure of payments that flow between any individual country and all other countries. *See* JOHN CHARLES POOL & STEVE STAMOS, THE ABCS OF INTERNATIONAL FINANCE, 25-28 (1987). It is used to summarize all international economic transactions for a particular country in a fixed time period. *Id.*

20. IEA ARTICLE, *supra* note 16. Many would argue that the United States is already feeling these three effects. *See* Dyer, *supra* note 16; *see also* Marc Vielle & Laurent Viguier, *On the Climate Change Effects of High Oil Prices*, 35 ENERGY POLICY 844 (2007).

> Oil prices shocks have a stagflationary effect on the macroeconomy of an oil importing country [as] they slow down the rate of growth (and may even reduce the level of output—i.e. cause a recession) and they lead to an increase in the price level and potentially an increase in the inflation rate.

Id.

21. IEA ARTICLE, *supra* note 16. The more sudden and pronounced the oil price increase, the greater these effects will be. *Id.*

22. *See* Hal S. Scott, *A Bankruptcy Procedure for Foreign Debtors?*, 37 INT'L LAW. 103, 127 (2003) (explaining that exchange controls are used to stem capital outflows and the accompanying downward pressure placed on exchange rates and exchange reserves).

23. *See* Callejo v. Bancomer, S.A., 764 F.2d 1101, 1104 (5th Cir. 1985) (stating that in response to a severe monetary crisis, Mexico imposed exchange controls which limited the number of pesos that foreigners could remove from the country and mandated that all deposits in Mexico banks be repaid in Mexican pesos at specific rates of exchange).

24. Gregory Meyer, *Crude Reaches $97 and Ends at a High*, WALL ST. J., Nov. 7, 2007, at C5.

25. *Id.*

the record high of $101.70 per barrel (adjusted for inflation), reached in April 1980.[26] The prospect of $100 per barrel oil seems likely amidst worldwide geopolitical tensions.[27] The U.S. dollar's devaluation reinforces these record oil prices.[28] The U.S. dollar has recently reached record lows against the euro,[29] the yen,[30] and the Canadian dollar.[31] Since oil is denominated in U.S. dollars, as the U.S. dollar loses its value, oil producers must maintain prices at a high enough level to avoid eroding their own purchasing power.[32]

A synopsis of the Oil Crisis of 1973 may add some clarity to the proposition that a huge increase in the price of oil will subsequently lead to the implementation of exchange controls by many developing countries.[33] In 1973, the price of oil quadrupled over several months as the Organization of Petroleum Exporting Countries ("OPEC") refused to sell its oil to countries that supported Israel in the Yom Kippur War.[34]

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26. Neil King, Jr., *Soaring Oil Prices Could Hit a Speed Bump*, WALL ST. J., Nov. 13, 2007, at A1.

27. *Id.*

28. *See* Riva Froymovich, *Dollar Fall Is Seen Continuing*, WALL ST. J., Nov. 5, 2007, at C7 (euro rises to its lifetime high). It should be noted that while the falling dollar has countless negative effects, it can also have various positive effects. *See, e.g.*, Timothy Aeppel, *Dollar Lifts Exporters, Blunting Housing Bust*, WALL ST. J., Oct. 1, 2007, at A1; Tyler Cowen, *The Dollar is Falling and That's Good News*, N.Y. TIMES, Dec. 2, 2007 ("The low value of the dollar has proved more a benefit than a cost.").

29. *See, e.g.*, Jonathan Cheng, *Flood of Money Strains Hong Kong's Dollar Peg*, WALL ST. J., Nov. 1, 2007, at C1 (U.S. dollar has decreased nearly 20% against the euro in the past two years); Mark Gongloff, *Unloved Dollar Might Just Win Favor Again*, WALL ST. J., Nov. 14, 2007, at C1 (U.S. dollar has tumbled 44% against the euro since 2002); Riva Froymovich, *Dollar Drops Further vs. Euro on Rate Cut*, WALL ST. J., Nov. 1, 2007, at C6 (U.S. dollar dropped to its seventh straight low against the euro and the Canadian dollar is trading at its modern-day high against the U.S. dollar).

30. *See* Joanna Slater & Riva Froymovich, *Dollar Hits Two-Year Low vs. Yen*, WALL ST. J., Nov. 13, 2007, at C2 (noting that one U.S. dollar buys 109.67 yen, a 7.2% decline from a year ago).

31. *See* Joanna Slater & Douglas Belkin, *Loonie's Rise Yields Splitting Pain for Canada*, WALL ST. J., Nov. 12, 2007, at C1 (noting that one Canadian dollar buys more than $1.10 in U.S. currency, a 24% decline since the start of 2007).

32. *See* Joanna Slater & Craig Karmin, *Markets Tumble as Dollar's Fall Adds to Anxiety*, WALL ST. J., Nov. 8, 2007, at C20.

33. The relative lack of new exchange controls implemented as a result of the 1973 crisis can be explained by the fact developing countries' economies now depend on oil far more than they did in 1973. *See* IAE ARTICLE, *supra* note 16, at 2.

34. *See* CBC News, *The Price of Oil: Marching to $100?*, July 18, 2007, http://www.cbc.ca/news/background/oil.

This rapid price increase resulted in a global economic downturn.[35] The U.S. experienced rampant inflation, increased unemployment, and finally, a recession.[36]

These devastating effects felt by one of the wealthiest nations in the world portray how even a prosperous nation can encounter trouble in the face of exorbitant oil prices. A sudden increase in the price of oil would lead to similar effects on all countries that import a substantial quantity of their oil, albeit to varying degrees depending on the wealth of the individual country.[37] The effects of a spike in oil prices, reminiscent of the Oil Crisis of 1973, would be overwhelming for developing countries, as their economies are now far more dependent on oil.[38]

Countless events could trigger a rapid increase in the price of oil (e.g., war with Iran, Venezuelan embargo, OPEC embargo,[39] terrorism, natural disasters).[40] Further, as the booming economies of India and China increase their demand for oil, worldwide demand will also continue to grow.[41] Predictions indicate Chinese and Indian energy consumption will double from 2005 to 2030,[42] in part because of increased demand for automobiles.[43] Even a small disruption in the

35. *See id.* Another possible reason for the increase in the price of oil and the subsequent recession was the decision by the United States (and Britain) to pull out of the Bretton Woods Accord, which took the U.S. off the Gold Standard. *See* David Hammes & Douglas Wills, *Black Gold: The End of Bretton Woods and the Oil-Price Shocks of the 1970s*, *available at* http://ssrn.com/abstract=388283. The result was a depreciation of the U.S. dollar as the U.S. increased its dollar reserves. *Id.*

36. *See id.*

37. *See infra* Part II.

38. *See* IAE ARTICLE, *supra* note 16, at 2.

39. OPEC countries supply about 40% of the world's oil demand. Neil King, Jr. & Ann Davis, *Oil Falls to $91 as Data Suggest Demand Shift*, WALL ST. J., Nov. 14, 2007, at A1.

40. For the sake of breadth and clarity, this Note only elaborates on a few of the many potential causes of a sudden spike in the price of oil.

41. *See* Jad Mouawad & Julia Werdigier, *Warning on Impact of China and India Oil Demand*, N.Y. TIMES, Nov. 7, 2007.

> [The] International Energy Agency warn[s] that [the] demand for oil imports by China and India will almost quadruple by 2030 and could create a supply 'crunch' as soon as 2015 if oil producers do not step up production, energy efficiency fails to improve and demand from the two countries is not dampened.

Id.

42. *See id.*

43. *See* Gordon Fairclough, *In China, Chery Automobile Drives an Industry Shift*, WALL ST. J., Dec. 4, 2007, at A1 (revealing that the number of automobiles in China has roughly doubled since 2004).

supply of oil seems to suggest a huge increase in the price of oil.[44] Some experts even postulate that oil production has already peaked[45] and that the world's oil supply is already running out.[46] If this theory gains general acceptance and proves true, the price of oil may skyrocket, as increased demand coupled with a diminishing supply equals sky-high prices.[47]

II. EFFECTS OF OIL PRICE INCREASE

As the price of oil continues to climb, the effects on developing countries are most severe, since wealthier countries are better positioned to withstand the shock.[48] The term "developing countries" is used generally, but more precisely refers to "oil-dependent developing countries" who import more petroleum than they export,[49] and typically use their energy less efficiently.[50] For example, oil-importing

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44. *See* King & Davis, *supra* note 39 ("A security scare, cutoff in supply, or shift in sentiment could send prices soaring again.").

45. *See, e.g.*, *World at Peak Oil Output*, CNN.com, http://edition.cnn.com/2007/BUSINESS/10/24/oil.decline/index.html (recounting how the Energy Watch Group postulates that worldwide oil production peaked in 2006 and will be half of what it is now by 2030); *see generally* David J. Lynch, *Debate Brews: Has Oil Production Peaked?*, USA TODAY, Oct. 16, 2005 (describing how the jury is still out on worldwide oil production).

46. *See* Lynch, *supra* note 45.

47. *See* Russell Gold & Ann Davis, *Oil Officials See Limit Looming on Production*, WALL ST. J., Nov. 19, 2007, at A1. The article quotes many oil industry chiefs as acknowledging that the number of barrels of crude oil that can be pumped is nearing, or at, current limits. *Id.* An oil production plateau would ensue which would "set the stage for a period marked by energy shortages, high prices and bare-knuckled competition for fuel." *Id.*

48. *See* IAE ARTICLE, *supra* note 16, at 2; *see also* Keith Johnson, *Americans Drive On, Despite $100 Oil*, WALL ST. J., Nov. 7, 2007, *available at* http://blogs.wsj.com/energy/2007/11/07/americans-drive-on-despite-100-oil (noting how Americans have not cut back on consumption despite record high gas prices as evidenced by the "80-cent-per-gallon increase at the pumps this year [that] hasn't really dented consumption").

49. The line demarcating developing countries as net-importers is extremely blurry, as some countries lack adequate refining capabilities, whereby they export oil, only to subsequently import that same oil in a more refined state. Other countries import/export different types of petroleum (e.g., light crude, heavy crude, natural gas). *See*, *e.g.*, Nazila Fathi, N.Y. TIMES, June 28, 2007 ("Iran is OPECs second-largest exporter of oil. But it needs to import half of its gasoline—at a cost of $5 billion a year—because of high consumption and low refining capabilities.").

50. *Id.*; *see* IAE ARTICLE, *supra* note 16, at 2.

developing countries use more than double the oil that a developed country uses to produce one unit of economic output.[51] Rapid increases in the price of oil are highly likely to cause recessions in these developing countries.[52]

An illustrative situation occurred in Costa Rica in the late 1970s.[53] Increased oil prices forced Costa Rica down a path of hyperinflation, increased unemployment, and soaring debt.[54] The events culminated with an imposition of exchange controls by Costa Rica, which declared a moratorium on foreign debt payments as the country could no longer afford to pay.[55]

Currently, oil prices contribute to reduced economic growth rates, imbalanced trade, and increased inflation in African countries.[56] According to the African Development Bank,[57] higher oil prices will exert an even heavier toll on the finances of many oil-importing African nations.[58] High oil prices in Africa lead to higher unemployment, as companies in Africa attempt to reduce their expenses by dismissing workers.[59] The situation further hurts the governments of these nations

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51. IAE ARTICLE, *supra* note 16, at 11.

52. *See High Oil Prices Disastrous for Developing Countries*, BIOPACT, Sept. 12, 2007 [hereinafter *High Oil Prices*] ("High oil prices are outright disastrous for developing countries and [the effects] are already hitting them.").

53. *See* Gilbert Brenes Camacho, *Left Behind in the Economic Crisis: Poverty Among the Elderly in Costa Rica* (Cal. Ctr. for Population Research, 2005), *available at* http://repositories.cdlib.org/ccpr/olcp/ccpr-cp-003-05/.

54. *Id.*

55. *See id.*; *see also* Libra Bank v. Banco Nacional de Costa Rica, 570 F. Supp. 870, 897 (S.D.N.Y. 1983) (explaining how Costa Rica imposed exchange controls).

56. *See High Oil Prices*, *supra* note 52.

57. "The African Development Bank (ADB) is a regional multilateral development finance institution established in 1964 and engaged in mobilizing resources towards the economic and social progress of its Regional Countries (RMCs). It is headquartered in Abidjan (Cote d'Ivoire)." African Development Bank, http://www.afdb.org/portal/page?_pageid=473,968615&_dad=portal&_schema=PORTAL (last visited Jan. 27, 2008).

58. *See* African Development Bank Group, *Can Struggling African Economies Survive Escalating Oil Prices?*, *available at* http://www.afdb.org/portal/page?_pageid=473,1036251&_dad=portal&_schema= PORTAL [hereinafter *Struggling African Economies*].

59. *See id.* The effects of rising oil prices are by no means restricted to Africa. *See, e.g.*, Oil Prices Hit Hard Asia's Poor, United Nations Development Programme (Oct. 25, 2007), *available at* http://content.undp.org/go/newsroom/2007/october/soaring-oil-prices-asia-20071025.en (Asian countries most vulnerable to high oil prices are Maldives, Cambodia, Sri Lanka, and to a lesser extent, Malaysia and Thailand).

as their tax base erodes.[60] Lower employment, together with higher inflation rates, lowers the purchasing power of the aggregate workers, which ripples throughout the nation's entire economy.[61] The high inflation, together with growing trade imbalances, leads to currency depreciations.[62]

Burgeoning oil prices and its corresponding effects on the nation place incredible pressure on central banks to act.[63] Recession and subsequent collapses of local currencies exert additional pressure on governmental authorities to use monetary policy in an attempt to alleviate the problems.[64] These actions may take the form of exchange controls[65] that would protect the developing nation's faltering currency.

Almost every international exchange of goods or services requires the exchange of one currency for another.[66] In the context of project finance agreements, entities take preventative measures to meet the currency risk that flows from foreign exchange.[67] Denominating all aspects of a project in the same currency provides a natural hedge against adverse exchange rate fluctuations.[68] Many times, a deal is structured so that revenues, costs, and debt facilities are denominated in U.S. dollars. These measures, however, may not adequately protect against all adverse effects from a rapidly depreciating local currency. The developing country (the "Host Country") simply might not have enough (or permit the exchange of) local currency and/or U.S. dollars,[69] or might institute exchange controls to restrict the outflow of U.S.

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60. *See Struggling African Economies*, *supra* note 58.

61. *See id.*

62. *See, e.g.*, IAE ARTICLE, *supra* note 16, at 12.

63. *See S. Africa's Mboweni Frets on Oil as Fuel Costs Jump*, REUTERS AFRICA, Dec. 1, 2007, *available at* http://africa.reuters.com/business/news/usnBAN131280.html ("High international oil prices are a major concern for central banks."). South African Reserve Bank Governor Tito Mboweni is quoted as saying, "The key global challenge [Africa] face[s] is oil prices." *Id.*

64. *See id.*; *Struggling African Economies, supra* note 58.

65. *See supra* note 4 and accompanying text.

66. Keith Feiler, *Strong Dollar, Weak Dollar*, On Reserve: Federal Reserve Bank of Chicago, http://www.chicagofed.org/consumer_information/strong_dollar_weak_dollar.cfm (last visited May 10, 2008).

67. *See* Katharin C. Baragon, *Project Finance*, 18 TRANSNAT'L LAW 139, 157 (2004).

68. *Id.* ("Fluctuations in the exchange rate of currencies in which project is trading and/or borrows . . . may negatively affect the cash flow of the project.").

69. *Cf. id.* ("Other interference[s] . . . may prevent the project from servicing its debt in the currency . . . .").

dollars beyond its borders. A simplified example may prove beneficial. A financier sponsors a project in a Host Country for the construction of a coal-powered energy plant, owned and run by an operator. The project's debt, denominated in U.S. dollars, is to be repaid by the revenue stream collected by the operator from the end-users of the electricity. This requires the operator to exchange the local currency collected for U.S. dollars in order to service the debt to the financier. The time horizon on the project's repayment is fifteen years after completion of the project, at the current exchange rates (the financier has various hedging positions to effectively eliminate its currency risk). However, five years after the completion of the project, an event occurs that sends the price of oil skyrocketing.[70] The Host Country's economy declines and soon slips into a recession. Pressure mounts on the Host Country's government to maintain the integrity of its depreciating currency and combat currency outflow. Accordingly, the government institutes various exchange controls, including a restriction on the outflow of its local currency and its U.S. dollar reserves.[71] Therefore, the operator will be stuck with local currency that he cannot exchange with the Host Country, nor exchange on the foreign exchange market.

The original contract required exchange of the local currency for U.S. dollars, which now would violate an exchange control. Thus, the underlying contract may be rendered unenforceable per Article VIII(2)(b),[72] depending on the statutory interpretation of an exchange contract in the relevant jurisdiction.[73] The financier benefits if the contract is not viewed as an exchange contract (narrow interpretation), thus placing the contract out of the purview of Article VIII(2)(b) (which would view said contract unenforceable). Conversely, the Host Country and the operator, hoping to avoid liability, wants a broad interpretation of an exchange contract. Because the contract is "contrary to the

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70. *See supra* Part I.

71. *See, e.g.*, Libra Bank v. Banco Nacional de Costa Rica, 570 F. Supp. 870, 897 (S.D.N.Y. 1983) (providing a similar example where Costa Rica's central bank refused to let foreigners be paid in U.S. dollars pursuant to the newly enacted exchange controls). In addition, the project agreement probably includes a concessionary agreement with the central bank of the Host Country whereby the foreign exchange goes directly through them, so the exchange would be impossible. *See* Peter K. Nevitt & Frank J. Fabozzi, PROJECT FINANCING 22-23 (7th ed. 2000); Kimmo Mettala, *Governing-Law Clauses of Loan Agreements in International Project Financing*, 20 INT'L LAW. 219, 221-22 (1986).

72. *See* IMF Articles of Agreement, *supra* note 6, art. VIII(2)(b).

73. *See infra* Part III.

exchange control regulations"[74] of a member state, it would be unenforceable.[75] Vagueness in the IMF article will inevitably lead to disagreement concerning interpretation.

III. AN INTERPRETATION OF EXCHANGE CONTRACT MEANING

When a country implements exchange controls after a sudden political change, drastic economic change, or the nationalization of financial institutions, Article VIII(2)(b) frequently is invoked to invalidate private international contracts.[76] More often than not, the party defending against contract enforcement is located in a developing country or is the government of the developing country itself.[77] Courts have struggled with whether to construe an "exchange contract" within Article VIII(2)(b) narrowly or broadly.[78]

U.S. federal case law supports the narrow view that only contracts which entail the exchange of one currency for another constitute exchange contracts for purposes of Article VIII(2)(b).[79] *Libra Bank v. Banco Nacional de Costa Rica* is one of the most renowned cases to discuss the issue.[80] Banco Nacional, a bank wholly owned by the Costa Rican government, defaulted on $40 million in loans made by the plaintiffs.[81] Banco Nacional argued it could no longer honor the loan agreement as the Costa Rican government had passed exchange controls,[82] which prevented the repayment of a dollar-denominated loan

74. *See* IMF Articles of Agreement, *supra* note 6, art. VIII(2)(b).

75. Article VIII(2)(b) completely bars the enforcement of an illegal exchange contract in any IMF member state. Marks, *supra* note 10.

76. Marks, *supra* note 10, at 105.

77. *Id.*

78. *Id.* at 106.

79. *See, e.g.*, Libra Bank v. Banco Nacional de Costa Rica, 570 F. Supp. 870, 897 (S.D.N.Y. 1983).

80. *Id.*

81. *Id.* at 875. Previous high oil prices that led to a recession in the Costa Rican economy also contributed to the defaut. *See* Camacho, *supra* note 53.

82. *Libra Bank*, 570 F. Supp. at 875; *see also* Callejo v. Bancomer, 764 F.2d 1101 (5th Cir. 1985) (providing another common example of an exchange control). In 1982, Mexico, in response to a severe monetary crisis triggered by a decline in the worldwide price of oil, imposed an exchange control that limited the number of pesos that foreigners could remove from the country, and further mandated that all deposits in Mexican banks, regardless of denominations, were to be repaid in Mexican pesos at specified rates of exchange. *Id.* at 1106. This had the effect of severely devaluing American investors' deposits. *Id.*

to foreigners.[83] Banco Nacional further contended that the loan agreement was an "exchange contract" and therefore the newly instituted exchange controls, validly imposed by an IMF country,[84] rendered the pertinent contract unenforceable under Article VIII(2)(b).[85]

The court rejected this argument, finding that the loans in question were not "exchange contracts" and displaying unwillingness to expand the definition to include international loans.[86] The court viewed exchange contracts narrowly, expressing that an exchange contract is a "contract for the exchange of one currency against another or on means of payment against another."[87] The court refused to adopt an interpretation of the article which would "sweep in all contracts affecting any members' exchange resources" and render "considerable violence to the text of the section."[88]

The court ultimately held that a contract to borrow U.S. currency, which requires repayment in U.S. currency in the U.S., is not an exchange contract within the meaning of Article VIII(2)(b).[89] The broader view of an "exchange contract" as any contract that involves monetary elements and, thus subject to the IMF agreement,[90] has also been rejected by New York state court, in accord with the view taken by the Southern District.[91]

Based on the rationale of *Banco*, courts in the U.S. today would probably continue to narrowly view "exchange contracts" as only those contracts that stipulate the exchange of one currency for another

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83. *Libra Bank*, 570 F. Supp. at 875.

84. *See id.* Some disagreement existed as to whether newly enacted exchange controls should be applied retroactively to executory contracts, or if the article should only apply to contracts which are unenforceable at their start. *Id.* at 900; *see also supra* note 6 and accompanying text.

85. *Libra Bank*, 570 F. Supp. at 896-97. "Defendant contends that both the Untied States and Costa Rica are signatories of the Agreements, that each element of Article VIII, section 2(b) is present in this case, and that the loan agreement is unenforceable." *Id.* at 897.

86. *Libra Bank*, 570 F. Supp. at 896-97.

87. *Id.*

88. *Id.* at 898 (quoting Banco Do Brasil, S.A. v. A.C. Israel Commodity Co. Inc., 190 N.E.2d 235, 236 (N.Y. 1963)).

89. *Id.* at 900.

90. *See id.*

91. *See, e.g.*, Banco Do Brasil, S.A. v. A.C. Israel Commodity Co. Inc., 190 N.E.2d 235 (N.Y. 1963) (endorsing a narrow view of an exchange contract); J. Zeevi & Sons, Ltd. v. Grindlays Bank (Uganda), Ltd., 333 N.E.2d 168 (N.Y. 1975) (letter of credit is not an exchange contract).

currency.[92] This may account for why the use of Article VIII(2)(b) as a defense in the United States has all but disappeared since the *Banco* decision.

Policy could also influence how U.S. courts define exchange contracts.[93] A wealthy, developed country who lends billions of dollars per year would be at the mercy of developing, debtor nations who could abuse the system simply by using exchange control legislation to avoid otherwise valid financing commitments.[94] A narrow view of Article VIII(2)(b) favors lenders such as the U.S. and European Union countries.[95]

Although comprised of developed countries, historically E.U. members have counter-intuitively viewed the article broadly.[96] Courts in France and the Netherlands, for instance, have analyzed exchange contracts under a broad interpretation.[97] This interpretation defines exchange contracts as contracts that have as their essential nature an exchange of goods or services that impacts foreign exchange reserves available in that country.[98] Thus, any contract for the sale of goods or services involving a currency which would also lead to a decrease or increase in the foreign exchange reserves of the member state is considered an exchange contract.[99] In this broad notion of exchange contracts, virtually all contracts between parties residing in IMF member states could potentially have such an impact and be considered exchange contracts.[100]

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92. *See* Wegen, *supra* note 6, at 1937-38.

93. *See generally* Werner F. Ebke, *Article VIII, Section 2(b): International Monetary Cooperation, and the Courts*, 23 INT'L LAW 677, 691-92 (1989) [hereinafter Ebke, *Article VIII*].

94. Ralph Folsom, *Exchange Contracts under Article VIII, 2(b)*, 2 INTBUSTRAN § 31.27 (2d ed. 2007).

95. *Id.*; *see also* Marks, *supra* note 10, at 107 ("[L]ocal bias in favor of creditors in the United States and the United Kingdom . . . may better explain the international divergence in judicial interpretations . . . .").

96. *See, e.g.*, Lessinger v. Mirau, I.L.R. 725 (1975) (German court decision adopting a broad view of an exchange contract which includes loan agreements). Courts in the United Kingdom have traditionally viewed Article VIII(2)(b) similarly to U.S. courts—narrowly. *See* Marks, *supra* note 10, at 107.

97. *See* Marks, *supra* note 10, at 107.

98. Wegen, *supra* note 6, at 1937-38.

99. *Id.*

100. *Id.*

This broad interpretation seems to further the IMF's goals by including more contracts in the scope of Article VIII(2)(b). Joseph Gold,[101] former General Counsel and Senior Consultant of the IMF, was convinced that only a broad interpretation of Article VIII(2)(b) would help accomplish the IMF's "macro objectives and improve the stability of the volatile international monetary system."[102] Furthermore, he has argued that the narrow construction, adopted by the United States and England, has without exception unfairly favored domestic lenders over foreign borrowers.[103]

More recently, however, many of these European courts which historically adopted a broad view of Article VIII(2)(b) are changing their thinking.[104] In 1993 and 1994, the German Supreme Court held in three decisions[105] that international capital transfers, such as loan agreements, are not governed by Article VIII(2)(b).[106] As a result, it seems that now the article will only be applied to current transactions,[107] and not to international capital transfers (including international loan

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101. *See* Werner F. Ebke, *Sir Joseph Gold and the International Law of Exchange Controls*, 35 INT'L LAW. 1475, 1479 (2001) [hereinafter Ebke, *Exchange Controls*]. He postulates that since the intent of the article was to assist poorer nations, it follows that a broad interpretation should be recognized. *Id.*; *see also* J. Gold, *The Fund Agreement in the Courts: Volume II* 425 (1982).

102. Ebke, *Exchange Controls*, *supra* note 101, at 1479.

103. *See id.* at 1484.

104. *Id.*

105. *See* Bundesgerichtshof [BGH] [Federal Court of Justice] Nov. 8, 1993, 39 Recht Der Internationalen Wirtschaft [RIW] 151 (F.R.G) (1994); Bundesgerichtshof [BGH] [Federal Court of Justice] Feb. 22, 1994, 39 Recht Der Internationalen Wirtschaft [RIW] 327 (F.R.G) (1994); Bundesgerichtshof [BGH] [Federal Court of Justice] Jan. 28, 1997, 42 Recht Der Internationalen Wirtschaft [RIW] 426 (F.R.G) (1997). For a further analysis of two of these decisions see Werner Ebke, *Article VIII, Section 2(b) of the IMF Articles of Agreement and International Capital Transfers: Perspectives from the German Supreme Court*, 28 INT'L LAW. 761 (1994).

106. *See* Ebke, *Exchange Controls*, *supra* note 101, at 1484.

107. Current transactions are defined by IMF Article XXX(d):

> Payments for current transactions means payments which are not for the purpose of transferring capital, and includes, without limitation:
>
> (1) all payments due in connection with foreign trade, other current business, including services, and normal short-term banking and credit facilities;
>
> (2) payments due as interest on loans and as net income from other investments;
>
> (3) payments of moderate amount for amortization of loans or for depreciation of direct investments; and
>
> (4) moderate remittances for family expenses.

IMF Articles of Agreement, supra note 6, art. XXX(d).

agreements).[108] This philosophical change can be attributed to a desire to improve domestic financial markets and to increase protection for local creditors against exchange controls.[109] Another possible reason for this change might be that Germany, because of increased international lending, would benefit from a narrow interpretation.[110]

A broad interpretation would likely put the vast majority of financing contracts at risk in times of a national crisis and call into question the validity of many project finance agreements. While American courts are quite unlikely to expand their definition,[111] all countries have discretion to interpret the article independently, and local incentives and biases can influence their interpretation.

IV. MINIMIZING RISK OF AN UNCLEAR DEFINITION

A. What Can the IMF Do?

The IMF can, and should, adopt a clear definition of an exchange contract as it applies to Article VIII(2)(b) of the agreement.[112] In the absence of a clear definition from the IMF, courts in IMF member states have reached conflicting decisions in determining the enforceability of contracts challenged pursuant to the article.[113] Courts rely upon their own methods of construction to determine if the article applies to certain contracts.[114] An amendment of Article VIII(2)(b), or at the very least an interpretation of the article, would help to alleviate the lack of uniformity.

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108. *See* Ebke, *Exchange Controls*, *supra* note 101, at 1484.

109. *See id.*

110. *Id.* at 1484 ("[Germany] followed the view expressed by the court of other major capital exporting countries . . . .").

111. For the very hopeful and optimistic it should be noted that the high court of this country has not given a definition of an "exchange contract" and from my research it seems that there is one U.S. opinion (albeit a dissenting one) that endorses the broader view of an exchange contract. *See* Weston Banking Corp. v. Turkiye Garanti Bankasi, 442 N.E.2d 1195, 1204 (N.Y. 1982) (Meyer, J., dissenting).

112. *But see* Ebke, *Article VIII*, *supra* note 93, at 706-09 (providing an alternative view that an amendment is not necessary).

113. *See id.* at 700-03.

114. *Id.*

1. Amendment

The IMF must define this severely ambiguous article to bring certainty to financing agreements. An amendment to the IMF's Articles of Agreement would achieve this. Such an amendment requires three-fifths of the membership, holding eighty-five percent of the vote, to vote in favor of any potential amendment.[115] Any such amendment would automatically become binding upon all member states of the IMF.[116] This procedure, although arduous, is not unattainable. The United States, with approximately 16.79% of the IMF's voting power,[117] could take the lead and propose an amendment which would, based on its bias, emphasize the narrow interpretation.[118] The United States would need at least 107 additional countries to vote in favor of such an amendment.[119] As IMF voting power is distributed on the basis of economic factors, including members' GDP, current account transactions (trade volume), and official reserves, almost all of the wealthier countries would have to vote in favor of such an amendment.[120] The seven countries with the largest number of votes by percentage, as of November 8, 2007, are the United States (16.79), Japan (6.02), Germany (5.88), France (4.86),

115. IMF Articles of Agreement, *supra* note 6, art. XXVIII(a) ("When three-fifths of the members, having eighty-five percent of the total voting power, have accepted the proposed amendment, the Fund shall certify the fact by a formal communication addressed to all members."). Currently the United States, which has over fifteen percent of the vote, wields a de facto veto. *See* Richard Euliss, Note, *The Feasiblity of the IMF's Sovereign Debt Restructuring Mechanism: An Alternative Statutory Approach to Mollify American Reservation*, 19 AM. U. INT'L L. REV. 107 (2003).

116. *See* Sean Hagain, *Designing a Legal Framework to Restructure Sovereign Debt*, 36 GEO. J. INT'L L. 299, 344 (2005).

117. International Monetary Fund, IMF Members' Quotas and Voting Power, and IMF Board of Governors, http://www.imf.org/external/np/sec/memdir/members.htm [hereinafter IMF Voting Power].

118. While I do not express a personal opinion on which interpretation of the article should be adopted, it seems more likely that a majority of IMF Member States would support the narrow interpretation. Hence, I support the narrow interpretation solely based on the greater likelihood that it would be officially adopted by the IMF.

119. Since there are 185 Member States, and three-fifths need to vote in favor of such an amendment, 108 Member States is the minimum number needed to pass an amendment. *See* IMF Voting Power, *supra* note 117.

120. Scott, *supra* note 22, at 135.

United Kingdom (4.86), Italy (3.20), and Saudi Arabia (3.17).[121] In total, these countries control about 45% of the vote.[122]

A proposition to construe the definition narrowly is certain to face ardent opposition by the (developing) country most likely to utilize the article as a defense.[123] Developing countries, especially those sensitive to oil price fluctuations, will be opposed to this type of amendment, since they may be the most in need of the article in the future.[124] These countries would certainly prefer no amendment at all, leaving the parties to their own devices. Additionally, the IMF itself would probably object to an amendment that emphasizes the narrow view.[125] Nonetheless, consent from many countries with unstable currencies, who collectively hold very little voting power, is not essential.[126]

Based on voting power, however, it is highly unlikely an amendment would be passed which construes the article broadly.[127] Therefore, to realistically achieve the broad definition, the article must be left undefined. This scenario would leave the status quo intact and courts would have no binding precedent. Developing countries would certainly argue that the IMF intentionally left Article VIII(2)(b) vague and malleable in order to help developing countries in crisis.[128] On the other hand, wealthier countries would welcome an amendment interpreting exchange contracts narrowly, as it would add more certainty to contracts, while simultaneously favoring their interests.

The following amendment would conclusively bring uniformity in the application of Article VIII(2)(b).[129] Although famed IMF scholar Sir Joseph Gold would certainly disagree with the narrowness of the

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121. IMF Voting Power, *supra* note 117.

122. *Id.*

123. *See* Marks, *supra* note 10, at 105.

124. *See supra* Part II.

125. *See* Ebke, *Exchange Controls*, *supra* note 101, at 1479 (noting how a narrow interpretation would be "contrary to the Fund's goals and, at least in the long run, opposed to the interests of every single IMF member state").

126. *See* Scott, *supra* note 22, at 135. For instance, not one African country holds even 1% of the total voting power, and Mexico only holds 1.43% voting power. IMF Voting Power, *supra* note 117.

127. *See supra* notes 117-19 and accompanying text.

128. *See supra* note 101 and accompanying text.

129. *But see* Ebke, *Exchange Controls*, *supra* note 101, at 1486-87. Ebke argues that complete uniformity is impossible "given numerous textual and contextual difficulties inherent in Article VIII, section 2(b)" and that the goal of the article should be a "functional equivalence." *Id.*

following amendment,[130] he would applaud the uniform interpretation it would produce.[131] Developed countries, who are influenced by their huge lending communities, would welcome this amendment and likely vote for its acceptance.

> [Proposed] Addendum to Article VIII(2)(b) to be Codified as Article VIII(2)(b)(1):
>
> > This Article shall only apply to exchange contracts, as defined herein, made between members, their citizens, or any combination thereof. Exchange contracts are contracts or agreements, in which one currency is exchanged for, or one means of payment against, another currency.
>
> [Proposed] Article VIII(2)(b)(1).

This article will be published in five major languages to avoid any inconsistencies in its exact interpretation.[132]

2. Interpretation

In addition to the powers to amend, the Executive Board of the IMF also has the power to interpret the Articles of Agreement.[133] At first glance, this solution, rather than an amendment, seems like a more obtainable goal, as an official interpretation does not require a vote by member states.[134] On the contrary, evidence suggests that the Board is quite wary to use this power.[135] The issuance of an interpretation is a political step, which, given the conflicting politics of member states, is only utilized for an extraordinary reason.[136] Coincidentally, however,

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130. *See id.* at 1479.

131. *See id.* at 1483. Sir Joseph believed that international monetary cooperation and collaboration should not be left to the whims of national forces, but instead the IMF should work to close the gap between the micro motives of each State for the benefit of all Member States. *See id.* at 1486.

132. Normally, international agreements are drafted in at least five languages to permit comparison between the texts to discern the precise meaning. *See* Wegen, *supra* note 6, at 1933.

133. *See* IMF Articles of Agreement, *supra* note 6, art. XXIX.

134. *See id.*

135. *See* Ebke, *Article VIII*, *supra* note 93, at 697.

136. *Id.* Another possible reason for the lack of interpretations issued by the IMF is the make-up of the Executive Board. The Board is comprised largely of bankers and

one of the few interpretations issued by the IMF has concerned Article VIII(2)(b).[137] The interpretation, nevertheless, does nothing to explain what exactly an "exchange contract" is in the context of Article VIII(2)(b).[138] A new interpretation could shed some light on the precise definition of an exchange contract and encourage uniformity amongst member state's courts when analyzing Article VIII(2)(b).

Unfortunately, even this solution is not infallible.[139] The interpretation would only command persuasive authority, as the Executive Board's interpretations are not binding on the courts of the member states.[140] Since the goal is uniform application of the definition of an exchange contract, an amendment would be a better solution than an official interpretation by the IMF.

B. What Can the Parties Do?

1. Explicit Stipulation (Uniformity Agreement)

In light of the current lack of clarity on the definition, parties can explicitly stipulate what constitutes an exchange contract in their contract. For instance, where a developing country is a participant to a financing contract and the risk for exchange controls exists, the lender may wish that their contract be deemed not an exchange contract, under any circumstances. Such a clause can be negotiated. Furthermore, the parties may desire to adopt a definition of what exactly constitutes an exchange contract.

Although some commentary indicates that two parties cannot contract out of the purview of exchange control regulations,[141] parties

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economists, not lawyers. Thus, they do not see themselves as charged with the duty of creating or applying international monetary law. *Id.* at 697-98.

137. *See* International Monetary Fund, Selected Decisions and Selected Documents of the International Monetary Fund, Thirtieth Issue, *available at* http://www.imf.org/external/pubs/ft/sd/index.asp?decision=446-4 (click "Unenforce-ability of Exchange Contracts: Fund's Interpretation of Article VIII, Section 2(b), Document No. 446-4" hyperlink) (last visited Feb.1, 2008).

138. *See id.* The interpretation says that the IMF will advise as to whether a particular exchange control regulation is imposed consistently with the Fund Agreement, but does not define an exchange contract. *Id.*

139. *See* Marks, *supra* note 10, at 106 n.12.

140. *See* Ebke, *Article VIII*, *supra* note 93, at 698.

141. *See* Otto Sandrock, *Are Disputes Over the Application of Article VIII, Section 2(b) of the IMF Treaty Arbitrable?*, 23 INT'L LAW. 933, 936 (1989) ("[E]xchange control regulations are not only mandatory on the level of substantive law, they are also

could still agree to a precise definition of what constitutes an "exchange contract." This would not be contracting out of exchange control regulations. Instead, the two parties are just agreeing to an interpretation, and it would be up to the courts to apply this mutually agreed upon definition to the contract at hand. Even so, there are obvious limits. If a contract involves the exchange of U.S. dollars for Mexican pesos and that contract contains a clause that reads, "This contract is not an exchange contract," it is clear this clause would be unenforceable or void. However, in less obvious cases, such as international loan agreements, courts should give deference to parties agreeing to certain clauses in a contract, especially when the clauses are intended to clarify the definition of an unclear term. It is not certain, however, that courts will apply what the parties want, so this option is less reliable than an IMF amendment.

2. Choice of Law Provision

The parties in the contract could also stipulate the governing law that applies to the contract.[142] Lenders want to keep the contract out of jurisdictions where a broad view of Article VIII(2)(b) is recognized by the courts. To do this, lenders would choose a jurisdiction that recognizes Article VIII(2)(b) very narrowly and insert the relevant choice of law provision into the contract. Although this choice of law would not extinguish all potential ramifications of Article VIII(2)(b), it would limit its use as a defense.[143] Since regulatory laws (such as exchange control regulations) apply regardless of the choice of the parties,[144] choosing a jurisdiction that characterizes "exchange contracts" very narrowly would benefit lenders. The United States, and more specifically, New York,[145] seems like the natural choice. However, lenders and borrowers would almost certainly disagree upon

beyond the conflict of laws autonomy of the parties who cannot derogate from them by choosing a foreign law as the proper law of the their contract.").

142. These stipulations are never foolproof for, in the event of any dispute, one party will certainly fight vigorously against its validity.

143. For instance, if a contract governed by New York law was simply an agreement to exchange one currency for another, this contract would fall within the purview of the IMF article even under the narrowest of interpretations. Thus, the contract would be at the mercy of any exchange control regulations imposed by the contracting parties' countries, despite the New York choice of law.

144. *See* Mettala, *supra* note 71, at 228.

145. *See infra* notes 153-55 and accompanying text.

the specific choice of law considering their conflicting motives. Nevertheless, since the lender usually has greater bargaining power, the borrower may be at the mercy of the lender's choice of law provisions.[146]

These choice of law provisions are never fail-safe, subject to various defenses such as the Act of State Doctrine,[147] (except in the case of arbitration),[148] and other public policy considerations. In selecting a certain jurisdiction, a lender also runs the risk that it cannot satisfy a favorable judgment if the defendant has insufficient assets in that jurisdiction.[149] Furthermore, most jurisdictions impose at least a minimal public-policy type limitation on the autonomy of parties in selecting the choice of law jurisdiction.[150] A court may decline to enforce a choice of law provision if it flouts a public policy of the jurisdiction whose law would otherwise apply, if not for the

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146. This lack of bargaining power could be used as a springboard by the borrower to argue that the choice of law provision should not be upheld because of duress, undue influence, or unilateral mistake.

147. Although beyond the scope of this article, a brief description may be useful. The Act of State Doctrine generally holds that a court in one country will not examine the validity of an act of a foreign state, when the act purports to give effect to the public interests of that state. Mettala, *supra* note 71, at 233; *see also* Underhill v. Hernandez, 168 U.S. 250 (1897).

148. The United States has eliminated the Act of State defense in actions to enforce arbitration agreements. *See* 9 U.S.C. § 15 (1994) (Federal Arbitration Act). Whether or not arbitrators even have the power to decide if a contract is an exchange contract under Article VIII(2)(b) is debatable. *Compare* Wegen, *supra* note 6, at 1937 ("there [is] . . . debate on this issue"), *and* William Park, *Arbitration in Banking and Finance*, 17 ANN. REV. BANKING L. 213, 254 ("National courts might refuse to enforce arbitration agreements implicating exchange controls, on the ground that the subject matter is 'not capable of settlement by arbitration' under the New York Convention."), *with* Sandrock, *supra* note 141, at 939 ("It is clear, therefore, from the purposes of article VIII, section 2(b), that the rules enshrined in it not only have to be followed by the state courts of Member States, but also by arbitral tribunals sitting within their territories.").

149. Mettala, *supra* note 71, at 242.

150. *Id.* at 243-45; *see* Allen v. Lloyd's of London, 94 F.3d 923, 928 (4th Cir. 1996).

> Choice of forum and law provisions may be found unreasonable if (1) their formation was induced by fraud or overreaching; (2) the complaining party 'will for all practical purposes be deprived of his day in court' because of the grave inconvenience or unfairness of the selected forum; (3) the fundamental unfairness of the chosen law may deprive the plaintiff of a remedy; or (4) their enforcement would contravene a strong public policy of the forum state.

Id.

provision.[151] The court may require a reasonable nexus between the contract's subject and the jurisdiction chosen.[152] For this reason, New York is again the jurisdiction of choice.

New York law allows parties to a contract to agree that its laws will govern their rights and duties, whether or not the contract bears any reasonable relationship to New York.[153] Since New York jurisprudence is highly developed, choosing New York law provides greater predictability in litigation outcomes.[154] New York's narrow interpretation of exchange contracts is of great importance.[155] Parties to a contract, where New York law has been chosen, would be more certain of what constitutes an exchange contract.

Parties should also expressly decide upon the forum where disputes shall be heard. The interplay between governing law and choice of forum should not be underestimated. The choice of governing law made by the parties may very well be affected by the choice of forum.[156] Procedural rules are determined by the *lex fori*.[157] Accordingly, a foreign court could forseeably view Article VIII(2)(b) as a procedural rule and decline to apply New York's substantive rule concerning the article. As courts prefer applying domestic laws, instead of foreign laws, it is highly recommended for parties to chosen a forum that matches their governing law choice.[158]

Courts also may restrict the scope of a forum selection clause by viewing it as a nonexclusive consent to jurisdiction,[159] which would allow the court to impose its jurisdiction even in light of a contractual provision.[160] Parties should explicitly state in the contract that the forum selected is the exclusive, mandatory forum for all disputed matters concerning the contract. Since this choice of law provision still cannot

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151. *See generally Allen*, 94 F.3d 923; Lipcon v. Underwriters at Lloyd's, London, 148 F.3d 1285 (11th Cir. 1998).

152. Mettala, *supra* note 71, at 243-45.

153. *See* N.Y. GEN. OBLIG. LAW. § 5-1401 (McKinney 2001).

154. Mettala, *supra* note 71, at 242.

155. *See supra* note 91 and accompanying text.

156. Mettala, *supra* note 71, at 237.

157. "The law of the forum." *Id.*

158. *Id.* at 238. Sometimes, however, a lender is given no choice in the matter, as legislation in the borrower's country requires the choice of law to be the borrower's country. *Id.* at 243.

159. *See* Park, *supra* note 7, at 229.

160. *Id.*

guarantee the desired result, an IMF amendment remains the optimal solution.

CONCLUSION

Article VIII(2)(b) is often overlooked in financing arrangements. This Note attempts to show how this diminutive IMF article, if not treated with its deserved respect, has the potential to destroy financing contracts, especially in these times of global economic uncertainty. The prospect of a massive surge in the price of oil, and its corresponding effects on developing countries, is all the more reason why the IMF and individual contracting parties must take heed of this article.

An IMF amendment to clarify Article VIII(2)(b) is clearly the best option, and would eliminate all ambiguity (not to mention saving time, money, opportunity costs, and judicial resources), although this seems unlikely in the near future. Similarly, an interpretation by the IMF, although non-binding, would also serve to clarify. Alternatively, parties should cautiously insert choice of law and uniformity provisions into their financing contracts to remove some degree of uncertainty. Although this option does not guarantee success, it is certainly better than nothing at all. Article VIII(2)(b) should never be overlooked, but rather given the attention it rightfully deserves.